

A changing world

At the end of June, JPMorgan Worldwide Securities Services announced a deal with Threadneedle Investments to lift out the latter's back office services. Here, *Conrad Kozak*, global head of JPMorgan Securities Services, discusses with Hugo Cox the significance of outsourcing investment operations, and how the industry will evolve.



Conrad Kozak,
global head,
JPMorgan
Securities
Services.

HUGO COX: In recent years there has been a lot more interest in alternative asset classes. How important will servicing these emerging assets become to the industry?

CONRAD KOZAK: In the current market environment, the ability to process derivatives and to provide hedge fund administration is rapidly becoming essential. We are therefore investing a significant amount of time and effort in developing our capabilities to process not only derivatives, but also leveraged loans and the myriad requirements to support private equity funds. Equally important is the ability to provide the accounting for these alternative instruments really well - whether it is for derivatives, equities or bonds. As this adjacent space continues to evolve, I don't think that the industry, as a whole, is at the level where many providers are currently supplying these broad-based services extremely well. Therefore, there's an enormous opportunity for players like us to combine a really broad range of asset servicing capabilities with the ability to execute them incredibly well.

HUGO COX: What are the implications of the growing popularity of outsourcing among asset managers?

CONRAD KOZAK: Our current activity, focus and ability to execute from a solid investment operations outsourcing platform is a critical component of our service offering going forward. Outsourcing is important to us for two reasons: it is clearly what clients want, and it also allows us to get closer to our clients, which enables us to better understand their needs. The increasing importance of outsourcing is driven by a focus among asset managers on their core competency. As they look to focus on the business of asset management, they are increasingly looking to offload the investment, time and responsibility of processing those investments to service providers such as us.

This is especially true as the emergence of new asset classes, such as derivatives, face managers with huge investments to develop new systems to accommodate

these instruments. While managers have accounting systems in place for regular assets - which they can continue to invest in and customise with added functionality - these systems will not accommodate derivatives. So they can either invest in building new systems to process derivatives or they can work with us to fulfill those needs. From our perspective, this extra product capability is a valuable service that we can offer clients and an extra source of growth.

So a player like us needs to be able to provide a really solid investment operations outsourcing platform because that is what our clients are demanding. The additional benefit of this trend is that we are becoming more intimate with our client base, gaining a better understanding of their needs and evolving our products accordingly.

HUGO COX: With regard to the outsourcing strategy, what is your investment operations strategy - is it based on a lift-out model or a modular approach?

CONRAD KOZAK: We will maintain our outsourcing business as an integrated business. We aim to grow this business globally and to continue to build a scalable, multi-client platform in three worldwide locations - the UK, the US and South Africa. Rather than lift-out multiple asset management back offices and run them separately, we will employ a couple of core accounting engines and a set of messaging and other processing systems that will be built off a core platform and be common to all of our outsourcing solutions. As we grow our business it is crucial for us to minimise the amount of individual customisation by ensuring that the core systems we use in our three global locations have sufficient flexibility to cater to the requirements of our worldwide client base.

An important consequence of this position is that we must have sufficient discipline only to do the deals that make strategic sense, given our set of capabilities. The capabilities we are putting together have a high degree of flexibility and allow for customisation. How-

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ever, we will continue to on-board new clients in an integrated fashion and to leverage enhancements to the global systems of the core platform overall.

HUGO COX: Perhaps the distinction between lift out and modular isn't so useful going forward?

CONRAD KOZAK: The lift-out and modular approaches are not necessarily inconsistent. In the first case, we will only lift out a client's system for as long as it takes to convert and integrate it to our systems. Essential to this approach is having a mutual agreement with the client before you do the lift out. We are very clear with our clients that we have no interest in lifting something out and then acting as a facilities manager for a separately run entity.

By the same token, when it comes to the modular approach, if your modules are small enough then you can mix and match them to achieve a huge amount of customisation without needing to tinker with the platforms or processes themselves or to build anything new. Once we have 30 or 40 modules in place that can be combined appropriately, then we can deliver anything the asset manager needs going forward.

HUGO COX: I understand you are in the process of rolling out a new reporting system called Views.

CONRAD KOZAK: Views is a single standard data warehouse and reporting system that replaces a number of separate reporting engines, and presents the information in one portal, or view, to the client.

We spent a long time developing this, and we are now rolling it out quickly: it will extend to our entire product range by the end of the year. By then we will be able to deliver to our customers any data or accounting information via that single platform.

HUGO COX: How has it been received by your clients?

CONRAD KOZAK: The clients using Views are commenting very favourably. Notably, several respondents in the recent ISF Repo Survey of securities borrowers – where we scored top in both weighted and unweighted categories – specifically noted Views as a reason for our outperformance.

Supporting this information, provided on the views portal, is a full history of more than four million issues and multiple public indices. In addition the system allows users to create their own investment ledger and report their own cash forecasting. The Views reporting allows clients to have greater access to data and flexible report-writing capability, being able to choose and order data elements within reports.

HUGO COX: What are the key challenges facing global securities services providers in the current market and how are you working to address them?

CONRAD KOZAK: The nature of the business is changing as the focus moves from the core custody offering towards the other value-added services provided around that primary offering. In the past, the core of what our clients really valued related solely to the custody product. Now, while custody remains fundamental to our offering, clients are increasingly asking for what we can do in addition to this. On the one hand, this means increasing emphasis on reporting, performance measurement, transfer agency, compliance and various other analytical functions. On the other hand, this includes the specialised processing around separately managed accounts and private client accounts. Going forward, I think it will be the strength of the overall asset servicing activities that firms can offer that will differentiate the top service providers.

In particular, I see a couple of challenges facing providers today. The first involves continuing to develop innovative products to keep up with the speed at which the market is developing. The second is the ability to make the entire range of service capabilities easily available, and to clearly communicate that to clients. In the first case, service providers are faced with an increasingly complex set of requirements as the market continues to evolve. It is a constant challenge to keep up with the new instruments, new techniques, new risk management requirements and new demands in terms of client outsourcing – derivatives servicing being an example in each case. This is a challenge that any business in a vibrant industry has to adjust to successfully.

The second challenge involves how well we leverage our own firm – to make the resources of our entire global JPMorgan platform available to our clients in a joined up, cohesive manner. The key in this effort is ease of use – whether we are talking about our processing services, clearance and trading, FX or cash management capabilities – the real challenge is to deliver these products in a way that the client can access quickly and smoothly.

HUGO COX: What is your strategy towards finding new markets for the business? To what extent is the dominance of the US set to remain?

CONRAD KOZAK: I think the financial service providers that will succeed going forward will be those that successfully develop and operate in markets outside of the US. Successful companies will need to roll out their service operations to Western Europe, Eastern Europe and Asia Pacific. Many of the big American asset servicing banks have not been sufficiently global so far. A significant amount of our revenues and growth currently come from regions outside of the US. Taking a more global approach means increasing the number of markets in which we can hold securities, but also increasing the client coverage model in those markets. It's about developing the mind set to service our clients effectively in these new global markets rather than simply having the worldwide capabilities to service the assets. We recently took an important step in this direction by basing two of our four senior securities product executives in the UK. This global sensitivity, insight and focus will be essential to the growth of our key non-US business going forward. **E**